

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-853

HAROLD CRAMER, Custodian for
PATRICIA GAIL CRAMER,*Petitioner,*

v.

GENERAL TELEPHONE & ELECTRONICS CORPORATION,
LESLIE H. WARNER, THEODORE F. BROPHY,
JOHN J. DOUGLAS, WILLIAM F. BENNETT
and ARTHUR ANDERSEN & Co.,*Respondents.*BRIEF OF RESPONDENTS, GENERAL TELEPHONE & ELECTRONICS
CORPORATION, LESLIE H. WARNER, THEODORE F. BROPHY,
JOHN J. DOUGLAS, AND WILLIAM F. BENNETT, IN OPPOSI-
TION TO PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE
THIRD CIRCUIT

PETER M. FISHBEIN
STEVEN J. GLASSMAN
KAYE, SCHOLER, FIERMAN,
HAYS & HANDLER
425 Park Avenue
New York, New York 10022
(212) 759-8400
Counsel for Respondents,
Leslie H. Warner, Theodore F.
Brophy and John J. Douglas

PETER H. MORRISON
MORRISON, PAUL & BEILEY
110 East 59th Street
New York, New York 10022
(212) 593-0100
Counsel for Respondent,
William F. Bennett

DEAN C. ROHRER
SAMUEL J. WILSON
GENERAL TELEPHONE & ELECTRONICS
CORPORATION
One Stamford Forum
Stamford, Connecticut 06904
(203) 357-3062

JOHN G. HARKINS, JR.
PATRICIA L. FREELAND
PEPPER, HAMILTON & SCHEETZ
2001 The Fidelity Building
Philadelphia, Pennsylvania 19109
(215) 893-3000

Counsel for Respondent,
General Telephone &
Electronics Corporation

TABLE OF CONTENTS

	PAGE
Opinions Below	2
Jurisdiction	2
Rule of Civil Procedure Involved	2
Questions Presented	2
Counter-Statement of the Case	3

REASONS FOR DENYING THE WRIT OF CERTIORARI

I. The Dismissal Under Rule 23.1 for Failure to Make a Demand is in Harmony With the Decisions of Other Circuits and Presents No Important Question of Law for This Court's Determination	5
II. The Dismissal Below Without Granting Leave to Amend Does Not Present Issues Justifying Grant of Certiorari	9
CONCLUSION	10

TABLE OF AUTHORITIES

<i>Abbe v. Goss</i> , 411 F. Supp. 923 (S.D.N.Y. 1975)	8n
<i>Asher v. Harrington</i> , 461 F.2d 890 (7th Cir. 1972)	9
<i>Brick v. Dominion Mortg. & Realty Trust</i> , 442 F. Supp. 283 (W.D.N.Y. 1977)	8n
<i>Bricker v. Crane</i> , 468 F.2d 1228 (1st Cir. 1972), cert. denied, 410 U.S. 930 (1973)	9

PAGE

<i>Cathedral Estates v. Taft Realty Corporation</i> , 228 F.2d 85 (2nd Cir. 1955)	7
<i>deHaas v. Empire Petroleum Co.</i> , 286 F. Supp. 809 (D. Colo. 1968), <i>aff'd</i> , 435 F.2d 1223 (10th Cir. 1970)	7
<i>DeLoach v. Woodley</i> , 405 F.2d 496 (5th Cir. 1969)	9
<i>Dopp v. American Electronic Laboratories, Inc.</i> , 55 F.R.D. 151 (S.D.N.Y. 1972)	8n
<i>Foman v. Davis</i> , 371 U.S. 178 (1962)	9
<i>Jannes v. Microwave Communications, Inc.</i> , 57 F.R.D. 18 (N.D. Ill. 1972)	8n
<i>In re Kauffman Mutual Fund Actions</i> , 479 F.2d 257 (1st Cir.), <i>cert. denied</i> , 414 U.S. 857 (1973)	5, 6, 6n, 7
<i>Liboff v. Wolfson</i> , 437 F.2d 121 (5th Cir. 1971)	7
<i>Nelson v. Pacific Southwest Airlines</i> , 399 F. Supp. 1025 (S.D. Cal. 1975)	8n
<i>Nussbacher v. Continental Ill. Nat. B. & T. Co., Chicago</i> , 518 F.2d 873 (7th Cir. 1975), <i>cert. denied</i> , 424 U.S. 928 (1976)	6, 7
<i>Oldfield v. Alston</i> , 77 F.R.D. 735 (N.D. Ga. 1978)	8n
<i>Papilsky v. Berndt</i> , 59 F.R.D. 95 (S.D.N.Y. 1973), <i>appeal dismissed</i> , 503 F.2d 554 (2d Cir. 1974)	7n
<i>Walden v. Elrod</i> , 72 F.R.D. 5 (W.D. Okla. 1976)	8n

IN THE

Supreme Court of the United States

OCTOBER TERM, 1978

No. 78-853

HAROLD CRAMER, Custodian for
PATRICIA GAIL CRAMER,

Petitioner,

v.

GENERAL TELEPHONE & ELECTRONICS CORPORATION,
LESLIE H. WARNER, THEODORE F. BROPHY,
JOHN J. DOUGLAS, WILLIAM F. BENNETT
and ARTHUR ANDERSEN & Co.,

Respondents.

**BRIEF OF RESPONDENTS, GENERAL TELEPHONE &
ELECTRONICS CORPORATION, LESLIE H. WARNER,
THEODORE F. BROPHY, JOHN J. DOUGLAS, AND
WILLIAM F. BENNETT, IN OPPOSITION TO PETITION
FOR WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE THIRD CIRCUIT**

Respondents, General Telephone & Electronics Corporation ("GTE"), Leslie H. Warner, Theodore F. Brophy, John J. Douglas and William F. Bennett, respectfully pray that the Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit, filed by petitioner Harold Cramer, be denied.

Opinions Below

The opinions below are appended to the Petition herein as Appendices A and B.

Jurisdiction

The Court's jurisdiction is not contested.

Rule of Civil Procedure Involved

The Rule of Civil Procedure involved is Rule 23.1, set forth in Appendix D to the Petition herein.

Questions Presented

I. Was it within the discretion of the Court of Appeals to affirm the dismissal of the present stockholder derivative complaint brought against four members of a fourteen-member Board of Directors and the corporation's independent public accountants, on the ground of petitioner's failure to make a demand, where (i) the ten non-defendant directors were not even alleged to have been involved in any impropriety, (ii) several of the directors at the time suit was brought were not even members of the Board at the time the alleged improprieties occurred, and (iii) an Audit Committee of independent, non-defendant directors had investigated and reported to shareholders on the claims, but had not, at the time the complaint was filed, considered or determined whether or not the claims should be prosecuted?

II. Was it within the discretion of the Court of Appeals to affirm the dismissal of the complaint without granting

leave to amend, where amendment would have served no purpose?

Counter-Statement of the Case

Petitioner, custodian for a stockholder of GTE, commenced this stockholder derivative action, purportedly on behalf of the corporation, without making a demand on the Board of Directors to institute suit. At the time suit was brought, the GTE Board consisted of fourteen individuals, only four of whom were named as defendants in this action. Petitioner alleged that those four individuals and GTE's independent public accountants participated or acquiesced in, or failed to discover, certain questionable payments made on behalf of GTE.

The specific acts complained of were recited in a Report of an investigation conducted by the Audit Committee of GTE's Board of Directors to determine whether GTE or its subsidiaries or affiliates had made questionable payments in any of the countries in which they did business. That Report, a copy of which was distributed to all stockholders shortly before the complaint was filed, was annexed as Exhibit A to the complaint, and specifically incorporated therein by reference. (Petition, Exh. A, p. 19).

Petitioner seeks to excuse his failure to make demand by claiming, in wholly conclusory fashion, that the four individual defendants dominated the remaining members of the fourteen-member Board at the time suit was brought. He also suggests that futility of demand arises from the failure of the Audit Committee to recommend the institution of litigation.

Petitioner fails to address the indisputable facts which are inconsistent with his claim of futility, and were considered by the Court below, that the ten non-defendant

members of the Board had no involvement whatsoever in the alleged wrongdoing, and that several of the directors at the time suit was commenced had not even been members of the Board at the time of the alleged wrongdoing. (Petition, Appendix A, p. 43). Moreover the Audit Committee consisted of four outside directors who had not been involved in any of the alleged questionable transactions (*Id.* at 19-20). Petitioner's reliance on the supposed inaction of the Audit Committee upon completion of its Report misconceives its function. As the Court of Appeals noted, that Committee had been authorized to examine GTE's business transactions, disclose any questionable payments, and suggest internal procedures for remedying any questionable prior practices. (*Id.* at 20-21, 42). It was not instructed to, and did not determine, whether the corporation should institute any litigation as a result of any transaction under investigation. (*Id.*).* Accordingly, the Court of Appeals concluded that demand could not be excused here.

REASONS FOR DENYING THE WRIT OF CERTIORARI

I.

The Dismissal Under Rule 23.1 for Failure to Make a Demand is in Harmony With the Decisions of Other Circuits and Presents No Important Question of Law for This Court's Determination.

The Court of Appeals' affirmance of the dismissal below, on the grounds of petitioner's failure to make a demand or to plead facts sufficient to excuse a demand, presents no issues which merit the grant of certiorari. There is no conflict between the Circuits requiring this Court's attention, the issues presented are of no practical significance and are inappropriate for this Court's review. As petitioner describes the issues, they involve basically a question of pleading. To the extent that the issues go beyond a pleading requirement, and involve the substantive requirement of a demand under Rule 23.1, prior to institution of a stockholder derivative suit, they involve the application of the facts of each case to a rule of law formulated consistently from Circuit to Circuit.

The Petition is misleading in repeatedly referring to a supposed conflict in the decisions of the various Circuits, when most of the cases cited by petitioner are District Court opinions. Regardless, there is no conflict presented for this Court's resolution, either by the few Circuit Court decisions or the District Court decisions which are cited.

In re Kauffman Mutual Fund Actions, 479 F.2d 257 (1st Cir.), cert. denied, 414 U.S. 857 (1973), relegated to a footnote of the Petition (at p. 11 n. 9), presented a factual situation most analogous to that of the present case, and

* In fact, shortly after the present litigation was instituted, GTE established an independent Special Litigation Committee to determine this precise issue. (Petition, Exh. A, p. 22).

resulted in dismissal for failure to make a demand. In *Kauffman* it was generally alleged that the director-defendants dominated and controlled the Board, but as in the present case there were no supporting factual allegations, and the defendants constituted less than a majority of the Board. 479 F.2d at 264. Moreover, just as in the present case, there was no allegation that the non-defendant directors participated in the alleged wrongdoing. Consequently, the First Circuit held that demand was not futile at the time suit was brought, and dismissal of the complaint was affirmed. *Id.* at 263-64.* The First Circuit's decision in *Kauffman* is unquestionably fully consistent with the determination of the Third Circuit here.

Each of the Court of Appeals decisions cited by petitioner which excused demand is consistent with *Kauffman* and the present case, since each involved a majority of directors who had personally participated in the wrongdoing, or were nominees of and effectively controlled by the alleged wrongdoers through stock ownership.

For example, in *Nussbacher v. Continental Ill. Nat. B. & T. Co., Chicago*, 518 F.2d 873 (7th Cir. 1975), *cert. denied*, 424 U.S. 928 (1976), in which the Court upheld the plaintiff's contention of futility, the complaint alleged (unlike the complaint here) that a majority of the Board members at the time of suit had been personally involved in the claimed wrongdoing. 518 F.2d at 875. Moreover, this same Board had already resolved that such a suit should not be prosecuted by the corporation. *Id.* 518 F.2d at 875, 878. The Seventh Circuit specifically noted that its decision,

* In *Kauffman*, plaintiff also alleged approval of the transactions by the full board, but the Court found such allegations insufficient, absent self-interest or other indication of bias, to excuse a demand. 479 F.2d at 265. In the present case, the ten non-defendant members of the GTE Board did not even pass upon, let alone approve, the challenged transactions.

consistent with the First Circuit's *Kauffman* decision, was based on different facts which led to a different result. *Id.* at 879. The Third Circuit's decision in the present case, based on facts similar to *Kauffman*, is therefore fully consistent with *Nussbacher*. And indeed, the Third Circuit's opinion here specifically referred to and distinguished *Nussbacher* on its facts. There is therefore no conflict presented for this Court's resolution.

Similarly, *Liboff v. Wolfson*, 437 F.2d 121 (5th Cir. 1971), also cited by petitioner, excused demand because, unlike the present case, a majority of the board of directors participated, approved of and acquiesced in the alleged wrongdoing, and were therefore charged with liability. In *deHaas v. Empire Petroleum Co.*, 286 F. Supp. 809 (D. Colo. 1968), *aff'd*, 435 F.2d 1223 (10th Cir. 1970), demand was excused where, unlike the present case, the defendants had "absolute control over the elective process within the corporation." 286 F. Supp. at 814. In the only other Court of Appeals decision cited by petitioner for his supposed "conflict," *Cathedral Estates v. Taft Realty Corporation*, 228 F.2d 85 (2nd Cir. 1955), demand was excused where a majority of the members of the board were also directors of another entity directly involved in the alleged wrongdoing. Moreover, the individual defendants in *Cathedral Estates* held a 92% interest in the corporation, and the remaining directors were their nominees. None of these factors are present here.*

* The District Court cases cited by petitioner lend no further support to his position. Each of those decisions, excusing demand, was based on the presence of majority involvement in or specific approval of, wrongful acts, or facts showing domination and control of the majority by the alleged wrongdoers, unlike the present case. For example, in *Papišky v. Berndt*, 59 F.R.D. 95 (S.D.N.Y. 1973), *appeal dismissed*, 503 F.2d 554 (2d Cir. 1974), all directors were named as defendants, allegedly participated or acquiesced in the challenged transactions, and were personally liable. See also,

In short, the Third Circuit's decision here, affirming dismissal of the complaint for failure to make a demand, is in harmony with the decisions of all other Circuit Courts which have been faced with the issue. Put simply, the type of factual situation involved here was not one in which demand could be excused.

Moreover, the decision here, that demand could not be excused in these circumstances, cannot conceivably affect the substantive rights of anyone. The cause of action in a stockholder derivative case is that of the corporation, not an individual stockholder. Accordingly, either the corporation will bring a suit upon demand or, if the demand is rejected, the individual stockholder may then attempt to proceed with an action on behalf of the corporation. The only issue presented here is whether, given the facts of the present case, the corporation, acting through its Board of Directors, should have been given an opportunity to consider whether to institute litigation before a derivative suit was commenced by a single stockholder. The Third Circuit's exercise of its discretion to dismiss the complaint

Oldfield v. Alston, 77 F.R.D. 735 (N.D. Ga. 1978) (all trustees participated in wrongful acts or approved of them with full knowledge of their wrongful character, and all were named as defendants); *Brick v. Dominion Mortg. & Realty Trust*, 442 F. Supp. 283 (W.D.N.Y. 1977) (all directors participated in plan to defraud investors, and all were named as defendants); *Walden v. Elrod*, 72 F.R.D. 5 (W.D.Okla. 1976) (majority stockholders named as defendants); *Abbe v. Goss*, 411 F. Supp. 923 (S.D.N.Y. 1975) (defendants controlled Board through substantial stock ownership); *Nelson v. Pacific Southwest Airlines*, 399 F. Supp. 1025 (S.D. Cal. 1975) (majority of directors served on board at time of challenged transaction, and had personally approved transaction; defendant controlled Board through 79% stock ownership); *Jannes v. Microwave Communications, Inc.*, 57 F.R.D. 18 (N.D. Ill. 1972) (wrongdoing alleged on part of all directors); *Dopp v. American Electronic Laboratories, Inc.*, 55 F.R.D. 151 (S.D.N.Y. 1972) (defendants controlled Board through substantial stock ownership).

here does not present any issue remotely worthy of review by this Court.

II.

The Dismissal Below Without Granting Leave to Amend Does Not Present Issues Justifying Grant of Certiorari.

Petitioner's alternative issue for review, the Court of Appeals' failure to grant leave to replead, cannot justify certiorari. Whether to grant leave to replead is unquestionably within the sound discretion of the Court, even under all the authorities cited by petitioner. Here, leave was undoubtedly denied since it would have served no purpose. It is clear that petitioner could not satisfy Rule 23.1 by repleading, since all of the relevant facts had already been fully considered by the Court of Appeals, regardless of the lack of "particularity" of the pleadings. The failure to grant leave to amend the complaint was, therefore, necessarily within the Court's discretion. *See, e.g., Foman v. Davis*, 371 U.S. 178, 182 (1962); *Bricker v. Crane*, 468 F.2d 1228, 1233 (1st Cir. 1972), *cert. denied*, 410 U.S. 930 (1973); *Asher v. Harrington*, 461 F.2d 890, 895 (7th Cir. 1972); *DeLoach v. Woodley*, 405 F.2d 496 (5th Cir. 1969). That decision does not present important issues which should be reviewed by this Court.

CONCLUSION

For all the reasons set forth above, the Petition for a Writ of Certiorari should be denied.

Dated: December 29, 1978

Respectfully submitted,

PETER M. FISHBEIN
STEVEN J. GLASSMAN
KAYE, SCHOLER, FIERMAN
HAYS & HANDLER
425 Park Avenue
New York, New York 10022
(212) 759-8400
Counsel for Respondents,
Leslie H. Warner, Theodore F.
Brophy and John J. Douglas

PETER H. MORRISON
MORRISON, PAUL & BEILEY
110 East 59th Street
New York, New York 10022
(212) 593-0100
Counsel for Respondent,
William F. Bennett

DEAN C. ROHRER
SAMUEL J. WILSON
GENERAL TELEPHONE &
ELECTRONICS CORPORATION
One Stamford Forum
Stamford, Connecticut 06904
(203) 357-3062

JOHN G. HARKINS, JR.
PATRICIA L. FREELAND
PEPPER, HAMILTON & SCHEETZ
2001 The Fidelity Building
Philadelphia, Pennsylvania 19109
(215) 893-3000

Counsel for Respondent,
General Telephone &
Electronics Corporation